

No. 15434

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United States  
Court of Appeals  
For the Ninth Circuit

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AH PAH REDWOOD CO., a Corporation,  
Petitioner,  
vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

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Transcript of Record

**FILED**

**MAY - 8 1957**

**Petition to Review a Decision of the Tax Court  
of the United States**



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**Court of Appeals**  
*For the Ninth Circuit*

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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## APPEARANCES

KOERNER, YOUNG, McCOLLOCH &  
DEZENDORF,  
JAMES C. DEZENDORF,  
800 Pacific Bldg.,  
Portland 4, Oregon,  
For Petitioner.

CHARLES K. RICE,  
Asst. U. S. Attorney General;  
LEE A. JACKSON,  
Attorney, Dept. of Justice,  
Department of Justice,  
Washington 25, D. C.,  
For Respondent.





The Tax Court of the United States

Docket No. 50695

AH PAH REDWOOD CO., a California Corporation,  
tion,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Office of the Director of Internal Revenue, Lincoln Bldg., 222 S. W. Fifth Ave., Portland 4, Oregon, A:R:90D:ENH) dated June 18, 1953, and, as a basis of its proceeding, alleges as follows:

I.

The petitioner is a corporation organized under the laws of California whose mailing address is 1101 S. W. Fifth Ave., Portland, Oregon. The returns for the period here involved were filed with the Director of Internal Revenue for the District of Oregon.

II.

The notice of deficiency, a copy of which is attached hereto and made a part of this petition by reference, is dated June 18, 1953.

## III.

The taxes in controversy are income taxes for the calendar years 1947 to 1950, both dates inclusive, as follows:

1947	Tax	None	Sec. 291 penalty	None
1948	Tax	\$ 2,654.84	Sec. 291 penalty	\$ 663.71
1949	Tax	35,649.37	Sec. 291 penalty	8,912.35
1950	Tax	(665.38)	Sec. 291 penalty	(166.35)
		<hr/>		
Total.....		\$37,638.83	<hr/>	
			\$9,409.71	

## IV.

The determination of tax set forth in said notice of deficiency is based upon the following errors:

1. The Commissioner erred in increasing petitioner's income in each taxable year above cited by a redistribution of the capital gain on the sale of timber.

2. The Commissioner erred in the computation of the basis for and unit value of timber severed from the company's timber tracts.

## V.

The facts upon which petitioner relies are as follows:

1. The timber owned by petitioner is in the nature of a capital asset and is therefore entitled to the treatment applicable to capital gains and losses.

2. The basis for the computation of the gain or loss on the severance of timber is erroneous due to a large under-run experienced by petitioner and

redetermination of the basis is necessary to determine the true basis.

Wherefore, petitioner prays that the Court may hear the proceeding and:

1. Determine that the Commissioner erred in increasing petitioner's taxable income in the years above stated by a redistribution of the capital gain on sale of timber.

2. Determine that the Commissioner erred in determining the basis of timber severed by petitioner.

3. Grant such other and further relief as the Court may deem proper.

/s/ WM. F. MEYER,  
Counsel for Petitioner.

U. S. Treasury Department  
Office of the Director of Internal Revenue  
Lincoln Bldg., 222 S. W. 5th Ave.  
Portland 4, Oregon

June 18, 1953.

Ah Pah Redwood Co.,  
1101 S. W. Fifth,  
Portland, Oregon.

Dear Sirs:

You are advised that the determination of your income tax liability for the taxable years December

31, 1947, 1948 and 1949, discloses a deficiency of \$38,304.21 in tax and \$9,576.06 in penalty and that the determination of your income tax liability for the taxable year ended December 31, 1950, discloses an overassessment of \$665.38 in tax and \$166.35 in penalty, as shown in the statement attached.

A copy of this letter and statement has been mailed to your representatives, Mr. Wm. F. Meyer and Mr. A. L. Lukens, 538 Mead Building, Portland, Oregon, in accordance with the authority contained in the power of attorney executed by you.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with the Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday or legal holiday in the District of Columbia in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to Director of Internal Revenue, Audit Division,

Lincoln Building, 222 S. W. Fifth Avenue, Portland 4, Oregon. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency or deficiencies, and will prevent accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment whichever is earlier.

Very truly yours,

T. COLEMAN ANDREWS,  
Commissioner.

By /s/ R. C. GRANQUIST,  
Director.

Enclosures :

Statement

Form 1276

Agreement Form

Claim Form 843

DLM

Ah Pah Redwood Co.  
1101 S. W. Fifth  
Portland, Oregon

Income tax liability for the taxable years ended December 31, 1947, 1948, 1949 and 1950.

Years	Income Tax	Sec. 291 Penalty	Income Tax	Sec. 291 Penalty	Income Tax	Sec. 291 Penalty
1947	\$ 343.22	\$ 85.81	\$ 343.22	\$ 85.81	0	0
1948	6,356.01	1,589.00	3,701.17	925.29	\$ 2,654.84	\$ 663.71
1949	52,421.71	13,105.43	16,772.34	4,193.08	35,649.37	8,912.35
1950	4,165.89	1,041.47	4,831.27	1,207.82	(665.38)	(166.35)
Totals	\$63,286.83	\$15,821.71	\$25,648.00	\$6,412.00	\$37,638.83	\$9,409.71

In making this determination of your income tax liability, careful consideration has been given to the report of examination attached to the letter dated April 22, 1953.

Inasmuch as you failed to make and file a return for the taxable years 1947, 1948, 1949 and 1950, within the time prescribed by law, the 25 per cent of the tax has been added thereto in accordance with the provisions of Section 291 (a) of the Internal Revenue Code.

After processing, the overassessment shown herein will be applied in accordance with the provisions of Section 322(a) of the Internal Revenue Code, provided that you fully protect yourself against the running of the statute of limitations with respect to the apparent overassessment referred to in this letter, by filing with the Director of Internal Revenue for your district, a claim for refund on Form 843, a copy of which is enclosed, the basis



Adjustments to Income  
Year: 1947

Net income as disclosed by return, Form 1120.....	\$1,634.38
Unallowable deductions and additional income:	
(a) Ordinary income .....	2,826.19
	<hr/>
Total .....	\$4,460.57
Nontaxable income and additional deductions;	
(b) Capital gain .....	\$2,826.19
	<hr/>
Net income adjusted.....	\$1,634.38

Explanation of Adjustments

(a) It has been determined that the sale of timber held less than six months at a profit of \$2,826.19 is taxable as ordinary income instead of capital gain, your income is increased accordingly.

(b) Since the above adjustment was reported as a capital gain in the amount of \$2,826.19 your adjusted income is reduced by a like amount.

Computation of Tax

Net income adjusted.....		\$ 1,634.38
Normal tax: 15% of \$1,634.38....	\$ 245.16	
Surtax: 6% of \$1,634.38.....	98.06	
	<hr/>	
Income tax liability.....	\$ 343.22	
25% Delinquent Penalty.....		\$85.81
Tax and penalty previously		
assessed .....	343.22	\$85.81
	<hr/>	<hr/>
Deficiency .....	None	None

Taxable Year Ended December 31, 1948  
Adjustments to Income

Net income as disclosed	
by return .....	\$16,526.81
Unallowable deductions and additional income:	
(a) Ordinary income from	
sale of property.....	14,891.96
(b) Interest income .....	10,912.24
	<hr/>
Total .....	\$42,331.01

## Taxable Year Ended December 31, 1948—(Continued)

## Nontaxable income and additional deductions:

(c) Legal expense .....	\$ 15.00	
(d) Capital gain .....	14,891.96	14,906.96
		<hr/>
Net income adjusted.....		\$27,424.05

## Explanation of Adjustments

(a) It has been determined that the profit of \$14,891.96 from the sale of timber to Coast Redwood Co. is reportable as ordinary income instead of capital gain as reported in your return, your net income is increased accordingly.

(b) It has been determined that your interest income was understated on your return in the amount of \$10,912.24 and your net income is increased by such amount.

(c) Legal expense was understated in your return by the amount of \$15.00, and your net income is reduced by this amount.

(d) Since the \$14,891.96 (adjustment (a) above) was reported in your return as a capital gain in error, your adjusted income is reduced by a like amount.

## Computation of Tax—Alternative Method

Net income adjusted.....		\$ 27,424.05	
Less: Excess of net long-term capital gain over net short-term capital loss .....		5,511.57	
		<hr/>	
Normal and surtax net income .....		\$ 21,912.48	
Normal tax: 5,000.00x15% \$ 750.00			
15,000.00x17% \$ 2,550.00			
1,912.48x19% \$ 363.37	\$ 3,663.37		
Surtax: \$21,912.48x 6%	1,314.75		
	<hr/>		
Partial tax .....	\$ 4,978.12	Sec. 291	
Plus: 25% of \$5,511.57.....	1,377.89	Penalty	
	<hr/>		



## Computation of Tax—Alternative Method—(Continued)

Correct income tax liability and penalty .....	\$ 6,356.01	\$ 1,589.00
Income tax liability and penalty as disclosed by return, Account No. CP8-10011-52 .....	3,701.17	925.29
	<hr/>	<hr/>
Deficiency in income tax and penalty .....	\$ 2,654.84	663.71

## Taxable Year Ended Dec. 31, 1949

## Adjustments to Income

Net income as disclosed by return	\$ 59,260.61
Unallowable deductions and additional income:	
(a) Ordinary income from sale of property.....	17,564.14
(b) Capital gain adjust- ment .....	127,535.80
(c) Interest income .....	7,345.81
	<hr/>
Total .....	\$211,706.36
Nontaxable income and additional deductions:	
(d) Legal expense .....	275.00
	<hr/>
Net income adjusted.....	\$211,431.36

## Explanation of Adjustments

(a) It has been determined that your profit of \$17,564.14 (Sale Price \$82,972.27 less cost \$65,408.13) from the sale of timber to Coast Redwood Co. is reportable as ordinary income instead of capital gains, your income is increased accordingly. (Your return reported \$17,603.57 capital gain, a difference of \$39.43.)

(b) It has been determined that your capital gain on sale and repossession of

Foster Big Tree amounted to a total of \$194,625.17    \$194,625.17

Less: reported on the Foster Big Tree \$ 49,485.80

and less reported on Coast Redwood Co.

(see (a) above)..... 17,603.57    67,089.37

resulting in a net capital adjustment as

above of ..... \$127,535.80

and increasing your income by such amount.

(c) It has been determined that your income from interest was understated in the amount of \$7,345.81, and your income has been increased accordingly.

(d) It has been determined that your legal expense was understated in your return by the amount of \$275.00, your net income is reduced by such amount.

#### Computation of Tax—Alternative Method

Net income adjusted..... \$211,431.36

Less: Excess of net long-

term capital gain over net

short-term capital loss....

194,625.17

Normal and surtax net

income .....

\$ 16,806.19

Normal tax: \$ 5,000.00x15% \$ 750.00

11,806.19x17% 2,007.05 \$ 2,757.05

Surtax: 16,806.19x 6%

1,008.37

Partial tax .....

\$ 3,765.42

Sec. 291

Plus: 25% of \$194,625.17.....

48,656.29

Penalty

Correct income tax liability

and penalty .....

\$52,421.71

\$ 13,105.43

Income tax liability and

penalty as disclosed

by return, Account

No. CPS-10012-52 .....

16,772.34

4,193.08

Deficiency in income tax

and penalty .....

\$35,649.37

\$ 8,912.35

## Taxable Year Ended December 31, 1950

## Adjustments to Income

Net income as disclosed by return	\$ 21,005.51
Unallowable deductions and additional income:	
(a) Ordinary income from sale of property.....	4,930.08
Total .....	<u>\$25,935.59</u>
Nontaxable income and additional deductions:	
(b) Capital gain adjust- ment .....	7,823.01
Net income adjusted.....	<u>\$ 18,112.58</u>

## Explanation of Adjustments

(a) It has been determined that your profit of \$4,930.08 (sale price \$23,289.52 less cost \$18,359.44) from the sale of timber to Coast Redwood Co. is ordinary income instead of capital gains, your income is increased by such amount.

(b) It has been determined that your capital gain from sale of timber is \$24,094.89 instead of \$31,917.90, a difference of \$7,823.01, and your income has been reduced accordingly.

## Computation of Tax

Net income adjusted.....		\$ 18,112.58
Normal tax: \$18,112.58x23%	\$4,165.89	Sec. 291 Penalty
	<u>          </u>	<u>          </u>
Total income tax liability and penalty .....	\$4,165.89	\$1,041.47
Income tax liability and penalty as disclosed by return, No. CP8-10013-52 .....	4,831.27	1,207.82
	<u>          </u>	<u>          </u>
Overassessment of income tax and penalty .....	\$ 665.38	\$ 166.35

Duly verified.

Received and filed September 16, 1953, T.C.U.S.

Served September 17, 1953.

[Title of Tax Court and Cause.]

### ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, Kenneth W. Gemmill, Acting Chief Counsel, Internal Revenue Service, and for answer to the petition filed herein, admits, denies and alleges as follows:

1. Admits the allegations contained in paragraph I of the petition.

2. Admits the allegations contained in paragraph II of the petition.

3. Denies the allegations contained in paragraph III of the petition. Alleges that the deficiencies as determined by the Commissioner are in income tax and delinquency penalties for the taxable years 1948 and 1949, in the amounts as shown in the following tabulation, all of which are in dispute:

Year	Income tax	Delinquency Penalty
1948	\$ 2,654.84	\$ 663.71
1949	35,649.37	8,912.35

Specifically denies that there is in controversy, in this proceeding, any amount, whatsoever, of income tax or penalty for either of the taxable years 1947 or 1950.

4. Denies that he erred in his determination of the deficiencies in income tax and penalties as shown in the notice of deficiency from which the petitioner's appeal is taken. Specifically denies that

he erred in the manner and form as alleged in paragraph IV (1) and (2) of the petition.

5. Denies the allegations contained in paragraph V (1) and (2) of the petition.

6. Denies generally and specifically each and every material allegation contained in the petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, it is prayed that the petitioner's appeal be denied and that the Commissioner's determination of deficiencies be approved.

/s/ KENNETH W. GEMMILL,  
Acting Chief Counsel,  
Internal Revenue Service.

Of Counsel:

WOOLVIN PATTEN,  
Acting Regional Counsel;

E. C. CROUTER,  
Acting Appellate Counsel;

JOHN H. PIGG,  
Attorney, Internal Revenue  
Service.

Filed November 10, 1953, T.C.U.S.

[Title of District Court and Cause.]

## FINDINGS OF FACT AND OPINION

1. Held, the amounts received by petitioner in 1948 and 1949 from Coast Redwood Co. for Timber cut by the latter in those years from the property of petitioner are properly taxable as ordinary income.

2. Where petitioner did not in fact ascertain at any time during 1948 and 1949 a discrepancy between its actual timber resources and prior estimates, even though such fact was at times readily ascertainable, a revision of petitioner's depletion allowance effective for the years 1948 and 1949 is not warranted under section 23 (m), I.R.C. of 1939.

JAMES C. DEZENDORF, ESQ.,

For the Petitioner.

WENDELL M. BASYE, ESQ.,

For the Respondent.

The respondent determined deficiencies in income tax of petitioner, and additions thereto, pursuant to section 291(a) of the Internal Revenue Code of 1939, for failure to file timely returns, for years and in amounts as follows:

Year	Deficiency	Addition to Tax
1948	\$ 2,654.84	\$ 663.71
1949	35,649.37	8,912.35

Respondent's imposition of the additions to tax is not contested. Nor is error assigned with respect to various adjustments made by respondent in his de-



termination. The issues framed by the pleadings and here to be resolved are:

(1) Whether the amounts received by petitioner in 1948 and 1949 from Coast Redwood Co. for timber cut by the latter from the property of petitioner are properly taxable as long-term capital gains.

(2) Whether petitioner's depletion allowance for the taxable years 1948 and 1949 is properly to be adjusted subsequent to the close thereof by revision of the estimated amount of units of timber standing on petitioner's property during such years.

### Findings of Fact

The stipulation of facts filed by the parties, with exhibits attached, is adopted and, by this reference, made a part hereof.

The petitioner, Ah Pah Redwood Co., is a corporation organized under the laws of California, with its main office at Portland, Oregon. The returns for the periods here involved were filed with the then collector<sup>1</sup> of internal revenue for the district of Oregon. Such returns were filed on a calendar year basis.

Upon its organization in October, 1947, petitioner purchased all the right, title and interest of "the buyer" in a certain purchase agreement (herein-

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<sup>1</sup>The stipulation, as well as the petition, reads "Director," but this is obviously erroneous inasmuch as such office did not come into being until after the taxable years.

after called the Sage Agreement) and all the timber and land covered thereby, dated December 13, 1946, between Sage Land & Lumber Company, Inc., (hereinafter called Sage), as seller, and Union Bond & Trust Company (hereinafter called Union), as buyer. The timber and land involved are located in Humboldt County, California, and the purchase price paid by petitioner was \$1,443,838.99. Shortly after the purchase of this tract (hereinafter called the Sage Tract), petitioner, in October, 1947, under an oral or implied contract with Coast Redwood Co. (hereinafter called Coast), allowed the latter to begin cutting timber from the Sage Tract and pay therefor \$5.00 per thousand feet as removed. On January 9, 1950, petitioner entered into a formal written agreement with Coast, pursuant to which petitioner agreed to sell all of the timber and land covered by the Sage Agreement to Coast.

In the years, 1948 and 1949, petitioner reported its income on the sales of timber to Coast as long-term capital gains. In so reporting its income on the timber thus sold to Coast, petitioner used the basis for depletion of \$3.941566 per thousand board feet. Respondent also used such basis in computing a portion of the deficiencies here in question. This basis for depletion was computed by both parties by dividing the amount of timber on the Sage Tract, as was shown on Schedule A of the Sage Agreement per the French cruise, which amount petitioner assumed to be the correct quantity thereof, into the total purchase price paid by petitioner for such



agreement. In 1952, petitioner first became aware of the fact that Schedule A of the Sage Agreement erroneously overstated the quantity of timber on the Sage Tract by a substantial amount. Upon an actual cruise made shortly after logging operations ceased in November of 1954, it was ascertained that such overstatement was approximately double the actual amount and that there was a "fall-down" of approximately 48 per cent.

In addition to other sales, petitioner sold 33,883,000 board feet of timber covered by the Sage Agreement to A. K. Wilson Lumber Company in 1950. This quantity of timber was assumed to be the above amount on the basis of the quantities shown in Schedule A to the Sage Agreement. Prior to petitioner's acquisition of the Sage Agreement, International Pacific Pulp and Paper Co. sold 16,022,060 board feet of the timber covered thereby to Coast in the years 1946 and 1947.

### OPINION

Van Fossan, Judge: The first issue is whether the amounts received by petitioner in 1948 and 1949 from Coast for timber cut in those years by the latter from the Sage Tract are properly taxable as capital gains, as urged by petitioner, or as ordinary income, as determined by respondent. The statutes involved are sections 117 (j) (1) and 117 (k) (2) of the Internal Revenue Code of 1939, as amended, the

pertinent provisions of both of which are set forth below.<sup>2</sup> It is petitioner's position that the only question to be resolved under this issue is whether or not its oral arrangement with Coast, whereby Coast commenced logging operations on the Sage Tract, as indicated in our findings above, in October, 1947, shortly after petitioner's acquisition thereof, from

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<sup>2</sup>Sec. 117. Capital Gains and Losses.

\* \* \*

(j) Gains and Losses From Involuntary Conversion and From the Sale or Exchange of Certain Property Used in the Trade or Business.

(1) Definition of Property Used in the Trade or Business—For the purposes of this subsection, the term "property used in the trade or business" means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(1), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not \* \* \* (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business. Such term also includes timber with respect to which subsection (k) (1) or (2) is applicable \* \* \*

\* \* \*

(k) Gain or Loss Upon the Cutting of Timber.

\* \* \*

(2) In the case of the disposal of timber (held for more than six months prior to such disposal) by the owner thereof under any form or type of contract by virtue of which the owner retains an economic interest in such timber, the difference between the amount received for such timber and the adjusted depletion basis thereof shall be considered as though it were a gain or loss, as the case may be, upon the sale of such timber.

which logging operations the amounts in dispute were received, constituted a "disposal" by petitioner of all of the timber standing thereon within the meaning of section 117 (k) (2).

In line with this view, petitioner makes the argument on brief that such oral arrangement was ineffective to pass title to all of the standing timber in question in October, 1947, the date the oral agreement was made, because of the California Statute of Frauds (See §1091, West's Annotated California Codes (Civil); *Anderson vs. Palladine*, 178 P. 553; see, also, 34 Am. Jur. 498), and that it therefore could not and did not constitute a "disposal" of such timber within the ambit of the cited statute at any time prior to the execution of the written agreement in 1950. Further, petitioner advances the theory that while its oral agreement with Coast was not effective as a contract to sell standing timber, it did constitute a license to cut, which license ripened into a contract for the sale of logs upon the severance of each individual tree.

Whether or not petitioner's theory be valid, its application will not constitute a disposition of the issue framed in the pleadings. Thus to narrow the issue is to make the unwarranted assumption that the timber involved in the transaction at issue constituted a capital asset to petitioner at the time of such transaction, within the definition contained in section 117 (a) (1) of the Internal Revenue Code

of 1939,<sup>3</sup> or property used in petitioner's trade or business within the meaning of section 117(j) (1), *supra*. In this connection, respondent makes the point, which we feel to be well taken, that petitioner at no time engaged in any logging activities, but, rather, merely sold the Sage timber to others under arrangements whereby the vendees would do the logging; that these sales of timber were the only business activity entered into by petitioner; that it is thus to be considered as having been engaged in the trade or business of selling timber; and that the timber in dispute, whether or not it was standing, was held for sale to customers in the ordinary course of such business.

The facts found on this record lead to the conclusion that petitioner was engaged in the trade or business of selling timber and that the timber in controversy was held for sale to customers in the ordinary course thereof. Petitioner does not deny the nature of its business activity and the purpose for which the Sage timber was held. Nor does it claim that the timber comes within the definition of section 117 (a) (1), *supra*. In fact, petitioner bases its entire case upon the applicability of section

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<sup>3</sup>Sec. 117. Capital Gains and Losses.

(a) Definition—as used in this chapter——

(1) Capital Assets—The term “capital assets” means property held by the taxpayer (whether or not connected with his trade or business), but does not include \* \* \* property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business \* \* \*



117 (j), *supra*. In this connection, petitioner's position is summed up in its statement on brief that section 117 (j) " \* \* \* includes timber to which Section 117 (k) (2) is applicable and allows capital gain treatment of income therefrom without regard to the nature of the taxpayer's business or the purpose for which the timber is held." [Emphasis supplied.]

The view thus expressed is in direct conflict with the plain wording of the statute relied upon. Section 117 (j), by its own language, specifically excludes from its operation all property held for sale to customers in the ordinary course of business. This being true, the gains derived from the sale of the Sage timber, regardless of the time of such sale, would not qualify for capital gains treatment under either section 117 (a) (1) or section 117 (j).

While there is no direct evidence of the precise terms of the oral cutting contract entered into between petitioner and Coast, such contract, for aught that is shown, looked immediately to the severance and removal of all timber standing upon the Sage Tract. Under the provisions of the Uniform Sales Act which was enacted in California in 1931 (See Title 1, Sales of Goods, Stats. 1931, c. 1070, p. 2234, §1; §§1721-1800, West's Annotated California Codes (Civil, *supra*), the sale of "things attached to or forming a part of the land," which category includes *fructus naturales*, or standing timber, pursuant to a contract according to the terms of which the trees are to be severed and removed as soon

as possible, is a sale of goods, i.e., personalty, and not of an interest in land. See §1796, *supra*; Brown, *The Law of Personal Property*, 2d ed., §164. Thus it is, that, in our opinion, petitioner's cutting contract with Coast was fully enforceable by the latter in the California courts and not invalid for noncompliance with the Statute of Frauds. See § 1091, *supra*; see, also, §§ 1723, 1724, *supra*. By being allowed access to the Sage Tract and by beginning its logging operations, Coast partly performed on its contract with petitioner and by such partial performance removed the contract from the application of the Statute of Frauds. *McGinn vs. Willey*, 25 Cal. App. 303, 141 P. 49; cf. *Forbes vs. City of Los Angeles*, 101 Cal App. 781, 282 P. 528; 101 A.L.R. 923; see §1724, *supra*.

Accordingly, it is our view that petitioner's oral agreement with Coast, under either rationale, constituted a disposition of the Sage timber within six months of the acquisition thereof in direct opposition to the specific statutory language defining capital gains. See section 117(k)(2), *supra*, and footnote 2.

The recent case, *L. D. Wilson*, 26 T.C.—(June 7, 1956), is clearly distinguishable from that now before us. There the issues framed were whether the partnership, of which the petitioners therein were members, could be considered the "owner" of the timber in question within the intendment of section 117 (k) (2), *supra*, and, if so, whether the timber cutting arrangement involved was sufficient to constitute a "disposal" of the timber within the scope

of the statute involved. We answered both questions in the affirmative.

In the instant case, albeit the existing oral cutting arrangement between petitioner and Coast constitutes a valid cutting contract for the disposition of the Sage timber, such contract does not meet the prerequisites of a "disposal" within the statutory purview, in that at the time it was entered into, petitioner had been the owner of the Sage timber for a period of less than 6 months. Nor, contrary to the instant case, could the partnership in *L. D. Wilson*, *supra*, on the facts there present, be considered as having been in the trade or business of selling stumpage to customers in the ordinary course of such business.

In view of all the foregoing, respondent's determination on this point is affirmed.

The second issue involves petitioner's allegation that an erroneous basis for depletion was applied by both petitioner and the respondent to timber cut from its property in the taxable years.

The facts adduced herein show that the amount of recoverable units of timber standing on the Sage Tract was substantially less than the original estimate which was used in computing petitioner's depletion allowance at \$3.941566 per thousand board feet. Petitioner first became aware of the error in 1952 and upon an actual cruise made shortly following the cessation of logging activities in November, 1954, the amount of "fall-down" was ascertained to be approximately 48 per cent.

Petitioner here seeks revision of its depletion allowance for the years 1948 and 1949, citing section 23 (m), Internal Revenue Code of 1939,<sup>4</sup> and our opinion in *Marion A. Burt Beck*, 15 T.C. 642, affd. 194 F. 2d 537, as authorizing such adjustment. Petitioner reasons that since the amount of "fall-down" in its timber resources was readily ascertainable at all times during the taxable years, a revision of its depletion allowance should be made effective for those years. We do not agree.

The Beck case does not stand for the proposition advanced by the petitioner. There the taxpayer was contesting a downward revision by respondent of her depletion allowance for the years there involved. However, the record made in that proceeding was adequate to warrant our finding as a fact that the taxpayer on the basis of facts known and reasonably ascertainable in the taxable years had discovered the discrepancy between the amount of units of ore actually recoverable and the prior estimates thereof. This being true, we sustained respondent's action, saying, in part:

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<sup>4</sup>Sec. 23. Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

\* \* \*

(m) Depletion \* \* \* In any case in which it is ascertained as a result of operations or of development work that the recoverable units are greater or less than the prior estimate thereof, then such prior estimate (but not the basis for depletion) shall be revised and the allowance under this subsection for subsequent taxable years shall be based upon such revised estimate. \* \* \*



\* \* \* The statute does not imply that the party to whom it would be an immediate tax-wise advantage to suppress the information of a need for adjustment, has any privilege not to come forward and make the necessary correction in the return. \* \* \*

The evidence here affords us no basis for making any finding that petitioner at any time in the taxable years knew or even suspected that its prior estimate of standing timber was erroneous. Albeit such error was readily ascertainable, it was not in fact ascertained at any time within either of the taxable years. In our view, therefore, the revision sought by petitioner does not qualify under the statutory provision that the allowance "for subsequent taxable years shall be based upon such revised estimate." Cf. *Petit Anse Co. vs. Commissioner*, 155 F. 2d 797, certiorari denied 329 U.S. 732. Respondent's determination on this issue is approved.

Reviewed by the Court.

Decision will be entered for the respondent.

Murdock, J., dissenting:

The legislative history of section 117(k) indicates clearly that Congress was trying to give capital gains treatment to timber owners when they disposed of their timber. See *Helga Carlen*, 20 T.C. 573. This taxpayer seems to come precisely within the terms of section 117(k)(2) and, therefore, is entitled to its benefits.

I also have doubt on the depletion issue. The facts in regard to the true content were reasonably ascertainable during the taxable year, and under such circumstances a reasonable allowance for depletion could be based on such ascertainable facts.

Filed and entered September 28, 1956.

Served September 28, 1956.

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The Tax Court of the United States, Washington  
Docket No. 50695

AH PAH REDWOOD CO.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

### DECISION

Pursuant to the determination of the Court, as set forth in its Findings of Fact and Opinion, filed September 28, 1956, it is

Ordered and Decided: That there are deficiencies in income tax, and additions to tax, as follows:

Year	Deficiency	Addition to Tax Sec. 291(a)
1948	\$ 2,654.84	\$ 663.71
1949	35,649.37	8,912.35

EUGENE BLACK,  
Judge.

Entered October 28, 1956.

Served October 28, 1956.

In the United States Court of Appeals  
for the Ninth Circuit

Tax Court Docket No. 50695

AH PAH REDWOOD CO., a California Corporation,  
Petitioner,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

### PETITION FOR REVIEW

Ah Pah Redwood Co., the Petitioner in this cause, by James C. Dezendorf, counsel, hereby files its Petition for Review by the United States Court of Appeals for the Ninth Circuit of the decision entered by the Tax Court of the United States filed in this matter on September 28, 1956, 26 T.C. No. 149, determining deficiencies in Petitioner's federal income taxes for the calendar years 1948 and 1949 in the respective amounts of \$2,654.84 and \$35,649.37, resulting in additions to tax in the respective amounts of \$663.71 and \$8,912.35, and respectfully shows:

#### I.

Petitioner, Ah Pah Redwood Co., is a corporation duly organized and existing under and by virtue of the laws of the State of California, with its principal office being located at 1101 S.W. 5th Avenue, Portland, Oregon. The tax returns of Petitioner for the periods here involved were filed with the Collector of Internal Revenue for the District of Oregon, at his office in Portland, Oregon.

## II.

The controversy involves the proper determination of Petitioner's liability for federal income taxes for the calendar years 1948 and 1949.

The Petitioner, in October, 1947, acquired an interest in certain timber and land located in Humboldt County, California, from Union Bond & Trust Company. Under a purchase agreement dated December 13, 1946, Union Bond and Trust Company had contracted to purchase this timber and land from Sage Land and Lumber Company, Inc.

Shortly after the purchase of the land and timber above described, Petitioner entered into an oral or implied agreement with Coast Redwood Co., whereby the latter was permitted to enter upon the land and cut and remove the timber located thereon. Coast Redwood Co. was to pay purchaser \$5.00 per thousand board feet, as removed. All of the timber covered by the agreement with Coast Redwood Co. had been acquired by Petitioner from Union Bond and Trust Company under the agreement of October, 1947.

On January 9, 1950, Petitioner entered into a formal written agreement with Coast Redwood Co., pursuant to which Petitioner agreed to sell to Coast Redwood Co. all of the land and timber acquired by Petitioner from Union Bond and Trust Company in 1947.

For the years 1948 and 1949, Petitioner reported its income on sales of timber to Coast Redwood Co.

as long-term capital gains. On these sales, Petitioner used as a basis for depletion \$3.941566 per thousand board feet. This figure was obtained by using the amount of timber reputedly present on the tract as reflected in a timber cruise furnished Petitioner by Union Bond and Trust Company at the time the property was purchased. Until 1952, Petitioner assumed the amount of timber acquired was correctly stated in the cruise. In 1952, Petitioner realized that the figures relied upon had substantially overstated the amount of timber on the tract, and a new cruise completed in the winter of 1954-1955 indicated a "fall-down" of approximately 48 per cent.

The Commissioner of Internal Revenue held that gains realized by Petitioner from the sales of timber to Coast Redwood Co. should be taxed to Petitioner as ordinary income, and thereupon determined the deficiencies for the calendar years 1948 and 1949, as aforesaid.

### III.

Petitioner, Ah Pah Redwood Co., being aggrieved by the findings and conclusions contained in the findings and opinion of the Court, and by its decision entered pursuant thereto, desires to obtain a review thereof by the United States Court of Appeals for the Ninth Circuit.

/s/ JAMES C. DEZENDORF,  
Counsel for Petitioner.

Duly verified.

Received and filed December 18, 1956. T.C.U.S.



[Title of Court of Appeals and Cause.]

Tax Court Docket No. 50695

NOTICE OF FILING PETITION  
FOR REVIEW

To: Chief Counsel, Internal Revenue Service,  
Washington, D. C.

You are hereby notified that Petitioner, Ah Pah Redwood Co., on the 13th day of December, 1956, mailed for filing with the Clerk of the Tax Court of the United States at Washington, D. C., a Petition for Review by the United States Court of Appeals for the Ninth Circuit, of the decision of the Tax Court of the United States heretofore rendered in the above-entitled cause. A copy of the Petition for Review as filed is hereto attached and served upon you.

Dated at Portland, Oregon, this 13th day of December, 1956.

/s/ JAMES C. DEZENDORF,  
Counsel for Petitioner.

Affidavit of service by mail attached.

Received and filed December 18, 1956.

In the Tax Court of the United States

Docket No. 50695

**AH PAH REDWOOD COMPANY,**

Petitioner,

vs.

**COMMISSIONER OF INTERNAL REVENUE,**

Respondent.

Courtroom, U. S. Court of Appeals, U. S.

Court House, Portland, Oregon

May 9, 1955, Monday

The above-entitled matter came on for hearing,  
pursuant to notice to the parties, at 10:09 o'clock  
a.m.

Before: Honorable Ernest H. Van Fossan,  
Judge Presiding.

Appearances:

**MR. JAMES C. DEZENDORF,**

For the Petitioner.

**MR. WENDELL M. BASYE,**

For the Respondent.

### PROCEEDINGS

The Clerk: Docket Number 50695, Ah Pah Red-  
wood Company.

Mr. Basye: Wendell M. Basye, for the Respondent.

Mr. Dezendorf: James C. Dezendorf, for the Petitioner.

The Clerk: How do you spell your last name?

Mr. Dezendorf: D-e-z-e-n-d-o-r-f.

The Court: What is the situation in this case?

Mr. Dezendorf: We are ready.

The Court: How long do you estimate that it would take to try the case?

Mr. Dezendorf: Not over a half a day, I wouldn't think; would you?

Mr. Basye: No; I wouldn't think so.

The Court: It will await assignment.

Mr. Basye: We would like to have the case assigned toward the end of the calendar, your Honor, on the basis that we haven't been approached at all on stipulation of facts of the case.

Mr. Dezendorf: That will be agreeable with us.

The Court: I will consider that.

(Whereupon, at 10:12 o'clock a.m., the hearing in the above-entitled matter was taken under consideration by the Court, and subsequently set for trial which was called for at 2:00 o'clock p.m., Tuesday, May 10, 1955.)

The Clerk: Docket Number 50695, Ah Pah Redwood [3\*] Company.

Would the attorneys please state their appearances?

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\*Page numbering appearing at top of page of original Reporter's Transcript of Record.



Mr. Dezendorf: James C. Dezendorf, attorney for the Petitioner.

Mr. Basye: Wendell M. Basye, attorney for the Respondent.

The Clerk: William E.?

Mr. Basye: Wendell M.

The Clerk: Oh, Wendell M.

The Court: May I have your name again?

Mr. Dezendorf: Dezendorf—D-e-z-e-n-d-o-r-f.

The Court: Will you state the issues involved here?

Mr. Basye: Pursuant—if the Court please, pursuant to the provisions of Section 6861 of the Internal Revenue Code of 1954, the Respondent at this time asks leave to file with the Court, a Notice of Jeopardy Assessments, covering the deficiencies involved in this case.

The Court: That may be filed.

Mr. Dezendorf: If the Court please, the parties have entered into a stipulation which disposes of very many of the formal facts which Mr. Basye will present at the outset of his statement. There are only two basic questions involved in this proceeding, the first is whether the timber involved was disposed of within six months of the date of its acquisition, and the second is whether a proper completion basis or unit basis was applied to the timber that was [4] removed. We expect our evidence to show that the timber was not disposed within six months of the date of acquisition as is contended by the Government, because only an oral arrangement was in effect prior to the expiration of the six-month period,

and with respect to the completion basis, we expect to show that the Government's figures and the Petitioner's, too, were grossly inaccurate, because they were based upon a French cruise upon which the timber was purchased in the first place, which was compared with the timber that was sold and removed, and yet, while according to the French cruise, seventy million feet of timber should have remained when logging ceased, actually only thirty-seven million feet actually exists, so that there was approximately a fifty per cent fall-down in the cruise.

The Court: Mr. Basye, you may state the Government's position.

Mr. Basye: If the Court please, we feel that the issues as stated by the counsel for the Petitioner are not—we cannot quite narrow the case at the outset to those issues without further statement of facts. The position of the Government is, in accordance with the ninety-day letter, that the taxpayer, Petitioner in this case, was not entitled to treat sales of certain timber property or timber as a capital gain, and in view of the status of the petition filed by the taxpayer in this case, the assignment of errors in general, and the facts upon which the Petitioner relies are broad—very general—the allegations of error are broad, and until further facts can be submitted for the Court's consideration, we feel that the issues in the [5] case are first, did the Commissioner err in disallowing the capital gain treatment on the sales, and second, whether or not the cost or unit basis—or unit value of the timber was

in error. At this time, I would like to submit a stipulation of facts which the parties have agreed upon, together with Exhibit 1A, which purports to be an agreement between the Sage (phonetic) Land and Lumber Company, seller, and Union Bond and Trust Company, Exhibit 2B, which purports to be an agreement, between Ah Pah Redwood Company, as seller, and Coast Redwood Company as buyer.

The Court: The documents may be filed. They will be received.

Mr. Basye: The Respondent has no further statement of facts at this time.

The Court: You may proceed with the evidence.

Mr. Dezendorf: Mr. Adkins, will you step forward and be sworn, please?

J. J. ADKINS

a witness called on behalf of the Petitioner, first having been duly sworn, testified as follows:

The Clerk: Would you please state your name and address for the record?

The Witness: J. J. Adkins.

The Clerk: Is that A-d-k-i-n-s?

The Witness: Yes, mam.

The Court: What are the initials? [6]

The Witness: J. J.

Mr. Dezendorf: I wonder if I may have the exhibit that is on the table opposite the witness marked Petitioner's Exhibit 3?

The Court: What document is that?

Mr. Dezendorf: The map that is on the table, beside the witness.

(Testimony of J. J. Adkins.)

The Court: Hand it to the Clerk.

The Clerk: Maybe I had better go over there and mark it.

(Petitioner's Exhibit 3, witness Adkins, marked for identification.)

The Court: Is that marked for identification, Madam Clerk?

The Clerk: Identification.

The Court: Exhibit 3 for identification.

### Direct Examination

By Mr. Dezendorf:

Q. Mr. Adkins, your name is J. J. Adkins?

A. Yes, sir.

Q. And where do you live, Mr. Adkins?

A. Beaver Creek, Oregon.

Q. Mr. Adkins, what, if any connection did you have with the Sage B timber which was owned by the Petitioner, Ah Pah Redwood Company in Northern California? [7]

A. I was general superintendent for the Company.

The Court: Speak a little louder, Mr. Witness.

A. I was general superintendent for the Company.

Q. As general superintendent, were the logging operations under your direction and control?

A. Yes, sir.

(Testimony of J. J. Adkins.)

Q. When did you undertake your duties in that capacity?

A. Well, I started working for the Company—I started in as superintendent for the Company in 1936.

Q. And when did you have anything to do with this timber in Northern California?

A. First started going down there in about '47, I believe.

Q. And did you have charge of the logging operations there from 1947 on?

A. I was just on the verge until 1949.

Q. And what did you assume—what position did you assume with respect to the timber in 1949?

A. Full charge of the whole operation.

Q. How long did that continue?

A. Until March of 1954.

Q. And by whom are you now employed, Mr. Adkins?

A. Myself.

Q. During the course of your operations in the Sage B Timber, did you become intimately familiar with the timber standing on it, and the line involved? [8]

A. Yes, sir.

Q. Have you had occasion to be on the grounds since March of 1954?

A. I was in there in November of 1954 and I was also in there in February of '55.

Q. Mr. Adkins, drawing your attention to the map on the table beside you which has been marked as "Petitioner's Exhibit 3," can you tell us what that is?



(Testimony of J. J. Adkins.)

A. That is a map of the operation, showing logged off land, the land that has timber standing on it, the land that has felled and bucked timber on it, and the land that has cold decks, or where it's cold decks.

Q. Now, does this map show all of the area which is comprised within the Sage B lands?

A. No; there was some land in twelve one, that is Township Twelve North and One East.

Q. And what is the status of the timber that was on the Twelve One East that you have just mentioned. Is that still standing, or is that—— (Interrupted.)

A. No; that is all logged. That is the reason we—the map got so big we didn't use it.

Q. And the map which is Petitioner's Exhibit 3, shows all of the land on which there is any timber remaining, is that correct? A. Yes, sir.

Q. Was that map prepared under your supervision and control? A. Yes, sir. [9]

Q. Mr. Adkins, as of what date was—does that map speak, in other words, to what date has it been brought up to date?

A. That would be almost right up to date now. I would say within thirty days from now.

Q. When did logging operations on the area represented by the map cease?

A. In November of '54.

Q. And have there been any logging operations carried on since then?

A. No; no, there hasn't. There was some logging



(Testimony of J. J. Adkins.)

operations in there, but it involves something that isn't on there. With them two blank forties there.

Q. I see. We will offer the exhibit in evidence.

The Court: Any objection?

Mr. Basye: No objection.

The Court: It will be received, Exhibit No. 3.

(Petitioner's Exhibit 3, witness Adkins, received in evidence.)

Q. Now, Mr. Adkins, when the logging operations ceased in November of 1954, how much timber remained on the Sage B land according to the French cruise?

A. About seventy million or a little bit more.

Q. And at the same time, that is in November of 1954 when logging operations ceased, how much timber actually remained upon the ground? [10]

A. I don't think over about thirty-five, thirty-seven million.

Q. Mr. Adkins, when did you first suspect that there was a fall-down in the amount of timber being cut as compared with the French cruise?

A. Some time in the year of '52, and I don't remember just exactly what part of the year.

Q. When was it first possible to determine the actual amount of fall-down of the cruise, Mr. Adkins?

A. Not until he shut down last year, and they ran a complete line through there on the cutting boundaries.

Mr. Dezendorf: You may cross-examine.

(Testimony of J. J. Adkins.)

Cross-Examination

By Mr. Basye:

Q. Mr. Adkins, you stated that you were general superintendent for the company, I don't quite understand what company is involved—what company did you mean?

A. Coast Redwood Company and Union Bond and Trust Company.

Q. And it is with respect to those companies that you started your employment in 1936 I take it?

A. No; in 1936, Union Bond was in existence, but, of course, Coast Redwood wasn't. I don't remember. I believe that Coast Redwood was organized probably in about '45 or '46.

Q. You had no connection with the Ah Pah Redwood Company?

A. Yes; I did have to this extent, that I was in charge of the timber of this whole area of timber here, administering the logging of [11] it, looking after it, trying to get the line surveyed, and such things.

Q. Do you know of your own knowledge, Mr. Adkins, what agreement existed between Ah Pah Redwood Company and Coast Redwood Company, with respect to timber?

A. No; I wouldn't say that I could answer that question.

Q. Now, Mr. Adkins, with respect to the map that has been introduced in evidence as Petitioner's Exhibit 3. You state that you prepared the map?

(Testimony of J. J. Adkins.)

A. An engineer working for me did.

Q. Under your supervision?

A. That's right.

Q. And as I understand it, this map was kept cumulatively?

A. That's right.

Q. As timber was logged off of the tract, different markings were made upon the map?

A. Yes. And—— (Interrupted.)

Q. And—I'm sorry, go ahead.

A. Let me—now, the outside boundaries of that map are pretty accurate, but the inside boundaries—the survey on that was did by Sage, and it was pretty slow to get it surveyed, so we got the outside boundaries, so we didn't get on somebody else. The inside of it, you can't have it too accurate.

Q. Well, with respect to this map, it now shows the situation with respect to the timber as of November, 1954, is that correct?

A. That's right. [12]

Q. And that there were no other operations on the property after 1954?

A. That's right.

Q. Now, I believe you testified, Mr. Adkins, with respect to—it was your opinion that there was a certain amount of timber standing on the property on November, 1954, is that correct?

A. That's right.

Q. Would you tell me again how much timber was there, according to your opinion?

A. In my opinion?

Q. Yes, sir.

(Testimony of J. J. Adkins.)

A. About thirty-five or thirty-seven million.

Q. And you ascertained that at what time? When did you decide that there were thirty—— (Interrupted.)

A. Say between November and February of this year.

Q. Of 1954 and 1955? A. Yes, sir.

Q. Now, Mr. Adkins, are you a cruiser?

A. Not a licensed cruiser; no.

Q. Did you make a scientific cruise to determine what timber was left on the property, or is this estimate with respect to what you kept on the map?

A. Yes, sir; I made a scientific—not only mine, but another man's opinion, because I was interested in buying the timber that was standing there. [13]

Q. And what was the basis for your determination?

A. I believe you will have to—I will have to have—I don't quite understand the question.

Q. I was wondering what you took into consideration in making your scientific estimate of the—— (Interrupted.)

A. Oh, I see—I presume you are asking what quality timber and one thing another. Anything that I thought I could sell that was merchantable today.

Q. Have you ever been on the payroll of Ah Pah Redwood Company? A. No.

Q. Mr. Adkins, could sales be made of this timber by Ah Pah without your knowledge? In other words, if any timber was sold off of this particular tract by Ah Pah Redwood Company, would you nec-

(Testimony of J. J. Adkins.)

essarily have knowledge of it, because of your position with respect to Coast Redwood?

A. I think I would; yes.

Mr. Basye: No further questions.

Mr. Dezendorf: That's all, Mr. Adkins. Thank you.

(Witness excused.)

Mr. Dezendorf: Call Mr. Max Herndon.

JAMES M. HERNDON

a witness called on behalf of the Petitioner, first having been duly sworn, testified as follows:

The Clerk: Will you please state your name and address [14] for the record?

The Witness: James M. Herndon.

The Clerk: H-e-r-n-d-o-n?

The Witness: Yes, mam.

The Clerk: James M.?

The Witness: Right.

Mr. Dezendorf: May I have this marked as Petitioner's Exhibit 4, please?

The Clerk: Are you going to use that map over there any more?

Mr. Dezendorf: No.

The Clerk: I wonder if I may have it?

Mr. Dezendorf: Surely. (Map handed.)

The Clerk: Petitioner's Exhibit 4 for identification.

(Petitioner's Exhibit 4, witness Herndon, marked for identification.)



(Testimony of James M. Herndon.)

Direct Examination

By Mr. Dezendorf:

Q. Mr. Herndon, what is your business or occupation?      A. Certified Public Accountant.

Q. Speak up so we can all hear you.

A. Okay.

Q. And do you practice alone or with someone else?      A. I am a member of a firm.

Q. And what is the name of that firm? [15]

A. Yergen and Meyer.

Q. And where do you office in connection with your practice?      A. Head office is in Portland.

Q. And are you in charge of one of the branch offices?

A. Yes; I am in charge of the Medford Office.

Q. Mr. Herndon, I am showing you what has been marked as "Petitioner's Exhibit 4," and I will ask you to tell us what that is?

A. Well, this is a schedule of timber that has been either sold or removed from the Sage B Tract as prepared from the information that has been made available to me.

Q. Now, will you just explain that Exhibit to us a little fuller, Mr. Herndon, so that we will fully understand it, in connection with your testimony concerning it?

A. Well, in the years, originally this contract was contract between Union Bond and Trust Company and Sage Land and Lumber Company, and in



(Testimony of James M. Herndon.)

1946 and '47, there were certain amounts of timber severed—sixteen million feet and some odd—they were severed while the contract was owned by—wait a minute. The contract was owned by International Pacific Pulp and Paper Company, which had acquired it from Union Bond and Trust Company, and during 1946 and '47, while International Pacific Pulp and Paper Company owned the timber, they allowed Coast Redwood Company to sever sixteen and some odd million feet from the tract. Then, in, I think it is October of 1947, the timber was—and the contract were transferred to the Ah Pah Redwood [16] Company, which is a wholly owned subsidiary of International Pacific Pulp and Paper.

Mr. Basye: I object, your Honor, to the witness' answering those questions before he is properly qualified to show that he had knowledge of these various transactions that he is testifying to, on the grounds that so far, he has only stated that he was a public accountant, and certain information was furnished to him.

The Court: I think a little further qualification would be helpful.

Mr. Dezendorf: Well, if the Court please, all that he has mentioned so far are the facts that are included in the stipulation.

The Court: Proceed. We are not going to argue about it.

Q. Yes, sir. Mr. Herndon, relating now to the 1947 item by Ah Pah on the Exhibit, where did you procure the information which is there contained?

(Testimony of James M. Herndon.)

A. From this ledger I have on my lap.

Q. And the ledger that you have on your lap, is that the original ledger of Ah Pah Redwood Company?

A. That's right.

Q. And the other figures, the 1948 by Ah Pah on through to how far on the ledger which is before you?

A. Through June 30th of 1954. [17]

Q. Now, I call your attention to one item of eighteen million five hundred and seventy-five thousand, and the second one, where did you procure the information with respect to it?

A. One of those entries was in the ledger itself, and the other one was—came to light while we were having—during this examination.

Q. And that is included in the stipulation, is it not?

A. That's right.

Q. Now, Mr. Herndon, what does the figure total, one hundred and sixty-one thousand nine hundred and ninety-nine—one hundred and sixty-one million nine hundred and ninety-nine thousand four hundred and eighty-six represent in the middle of the Exhibit?

A. Well, that represents the total timber that was either sold or removed by cutting during the period from the original date of the contract, I guess, to—through November of 1954.

Q. Now, what—where did you get the information that is basis of the next portion of the Exhibit that you have prepared?

(Testimony of James M. Herndon.)

A. Well, I have here a copy of a contract which I think has already been filed with the Court. It is a copy of the Sage Land and Lumber agreement with Union Bond and Trust Company, and amended to that or appended to it, are some three pages of the forty-acre tracts that were in the Sage Land and Lumber Company contract. And on that schedule has been marked by Mr. Wilson, the portions that are still virgin timber, and the portions that are partially logged. And from those cruises, or footages by forty-acre tracts, I have added [18] those up and determined that there were fifty-eight million nine hundred and ninety-three thousand left per the French cruise, and then, in the—for want of better information, for—I had to estimate that the partially logged portions contained approximately fifty per cent, and that would be another eleven million six hundred and forty-four thousand or a total of seventy million six hundred and thirty-seven thousand feet of timber remaining according to the French cruise.

Q. Now, may I interrupt you there for a moment, Mr. Herndon, were you informed that fifty per cent of the forties which were partially—strike that. Were you informed that of the forty-acre plots which were partially logged off, that one-half of the timber remained?

A. No; there were quite a number of them, probably twenty or so, forty-acre tracts, and they were in various stages of cutting; some were almost entirely logged, some were almost entirely standing, so for—in order to develop some figures on this, we

(Testimony of James M. Herndon.)

used the fifty per cent average on the partially logged tract.

Q. Now, will you explain to us the figures and the items represented on the bottom part of the Exhibit?

A. Well, the total timber per the original contract for the original cruise was three hundred and eighty-two million feet, and some odd, and from that we deduct what we can determine as remaining per the French cruise, and we arrive at a total of three hundred and eleven million six hundred and ninety-six thousand feet that should have been logged or sold off of the tract. [19]

Q. And what, if anything, have you done further with respect to the actual amount of timber sold and removed from the property?

A. Well, by deducting the actual amount logged and sold, we arrive at a figure of a hundred and forty-nine thousand six hundred and ninety-six thousand five hundred and fourteen feet of timber that could be classed as fall-down. In other words, it was not in the—the cruises did not cut out by that amount of footage.

Q. And what percentage did that determine to be?

A. Forty-eight point oh three per cent.

Mr. Dezendorf: You may cross-examine. Oh, pardon me. I will offer the Exhibit Number 4.

Mr. Basye: No objection.

The Court: It will be received, Exhibit Number 4.

(Testimony of James M. Herndon.)

(Petitioner's Exhibit Number 4, witness Herndon, received in evidence.)

Mr. Dezendorf: You may cross-examine.

Cross-Examination

By Mr. Basye:

Q. Mr. Herndon, this Exhibit that has been submitted as Petitioner's Exhibit 4, was prepared by you, is that correct? A. That's correct.

Q. When was it so prepared?

A. It was last Saturday.

Q. The basis upon which this Exhibit—Petitioner's Exhibit 4 was prepared, was from information that you received, from, [20] I believe you testified, Mr. Wilson? A. A portion of it was.

Q. Will you please further identify Mr. Wilson for us?

A. That's Mr. A. K. Wilson, who is the President of the Ah Pah Redwood Company.

The Court: Didn't hear you.

A. Mr. A. K. Wilson, who is the President of the Ah Pah Redwood Company.

Q. Have you worked for Mr. A. K. Wilson in any other capacity other than by being employed by Ah Pah Redwood? A. Yes, sir, I have.

Q. Is Mr. Wilson the President of Coast Redwood Company? A. To my knowledge, he is.

Q. Is Mr. Wilson the President of Union Bond and Trust Company? A. He is.



(Testimony of James M. Herndon.)

Q. Is Mr. Wilson the President of International Pacific Pulp and Paper Company?

A. He is.

Q. Do you know who is the President of the A. K. Wilson Lumber Company?

A. Mr. Wilson.

Q. And do you know whether Mr. A. K. Wilson is a partner in the A. K. Wilson Timber Company?

A. He is. [21]

Mr. Basye: I have no further questions.

Mr. Dezendorf: No further questions.

The Court: You are excused.

(Witness excused.)

Mr. Dezendorf: Petitioners rest.

(Petitioners rest.)

The Court: Will you please tell me where they got the name "Ah Pah," what does that mean?

Mr. Dezendorf: Well, it is an Indian name. It doesn't really mean anything, but it is associated in that Northern California country there, and that is the reason the name was adopted for the name of the corporate vehicle to hold the timber.

The Court: Petitioner rests?

Mr. Dezendorf: Yes.

Mr. Basye: The Respondent would like to call Mr. Charles Carpenter.



CHARLES E. CARPENTER

a witness called on behalf of the Respondent, first having been duly sworn, testified as follows:

The Clerk: Will you please state your name and address for the record?

The Witness: Charles E. Carpenter, 1404 N. E. 58th, Portland.

Direct Examination

By Mr. Basye: [22]

Q. Will you tell the Court, Mr. Carpenter, your occupation? A. Internal Revenue Agent.

Q. In connection with your occupation, Mr. Carpenter, are you familiar with the income tax returns filed by Ah Pah Redwood Company, for the tax years 1948 and 1949?

A. I was at one time.

Q. What is the basis of your familiarity with them?

A. I made an examination of those returns.

Q. In connection with such examination, what did it entail, as far as work is concerned on your part?

A. Well, it took a considerable amount of work.

Q. What was the nature of that work?

A. Well, auditing of all of the records up to that period.

Q. These records included what, Mr. Carpenter?

A. Well, the general ledger, receipts and disbursements, and this examination details jointly with other affiliated companies, in order to reconcile the

(Testimony of Charles E. Carpenter.)

various organizations together was what took more of the detail and made work of this examination, as this—this Company standing alone, its records cannot be difficult to examine.

Q. Did this examination entail contacting for information or for conversation, any of the officers of Ah Pah Redwood Company? A. It did.

Q. Which officers?

A. Mr. A. K. Wilson. [23]

Q. And he was the President of Ah Pah Redwood, is that right? A. That's right.

Q. In connection with your examination, did you find, or was any information made available to you with respect to an alleged under-run of the timber property on Sage B timber tract?

Mr. Dezendorf: If the Court please, I would have to object to that question for the reason and upon the ground that it is based upon a finding—whatever he found would be the best evidence, and not his conclusion as to what it was. If it was based upon a conversation with Mr. Wilson, I think we are entitled to know where and when the conversation occurred.

Q. I will rephrase the question. In connection with your examination, Mr. Carpenter, did you make a report? A. Yes.

Q. At the time you conducted your examination, you made notes and made a report?

A. That's right.

Q. Do you have in the courtroom a copy of your report? A. I do.

(Testimony of Charles E. Carpenter.)

Q. I hand you herewith, what purports to be an Internal Revenue Agent's report, with respect to Ah Pah Redwood Company, the date of the original being January 12th, 1953, could you identify this report?

(Report handed.)

A. That is a copy of my original report, yes. A copy made by our office. [24]

The Court: I can't hear you.

A. A copy made by our office.

Q. And in preparing this report, did you make any reference to an alleged under-run in the Sage B Timber Tract, in question in this proceedings?

Mr. Dezendorf: If the Court please, I would object to that, for the reason and upon the ground that whether he made reference to it or not has no material bearing on any issue in this case. The fact might have been mentioned or discussed, not mentioned in his report; whatever is in his report, it speaks as the best evidence rather than his testimony concerning it.

The Court: He may answer.

Q. You may answer.

A. Could I have the question again, then?

Q. I believe I asked you whether you made reference in your report to any alleged under-run that had taken place on the Sage B Timber Tract?

A. Yes, in discussing with Mr. Wilson this case, Mr. Wilson agreed to all of the adjustments, but

(Testimony of Charles E. Carpenter.)

couldn't agree—couldn't sign what we call an eight seventy agreement form, because at that time, he said that he was—thought there would be a vast under-run in this tract of timber, and that he was not free to make any determination of that under-run at that time, but that when and if he could put the figures together to determine that, he was sure that it would prove on a tax basis that he should be entitled to an under-run, and [25] that would wipe out the other adjustments substantiating the tax liability.

Q. And you stated that this—that the time this report was prepared, the date was January 1st, 1953?

A. That's right.

Mr. Basye: You may inquire.

Mr. Dezendorf: No questions.

The Court: You are excused.

(Witness excused.)

Mr. Basye: The Respondent rests, your Honor.

(Respondent rests.)

The Court: Any rebuttal?

Mr. Dezendorf: No rebuttal.

The Court: How much time do you wish for briefs?

Mr. Basye: If the Court please, I would like to suggest sixty days for simultaneous briefs, sir.

Mr. Dezendorf: That would be agreeable.

The Court: Sixty days will be allowed for simultaneous briefs; thirty days thereafter for replies.

The case is closed.

(Whereupon, at 2:40 o'clock p.m., the hearing in the above-entitled petition was closed.)

Filed June 1, 1955, T.C.U.S. [26]

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EXHIBIT No. 1-A

[Penciled in top margin]: This Copy was Typed by Al Carlson on Oct. 24, 1952.

Purchase Agreement

This Agreement entered into this 13th day of December, 1946, between Sage Land and Lumber Company, Inc., a corporation, organized under the laws of the State of New York, hereinafter called "Seller," and Union Bond & Trust Company, a corporation organized under the laws of the State of Oregon, hereinafter called "Buyer";

Witnesseth

Now, Therefore, in consideration of the premises and of the performance of the provisions of this Agreement, the parties hereto agree as follows:

1. Seller agrees to sell and Buyer agrees to purchase and take from Seller at the times and upon the conditions hereinafter set forth the lands situated in the County of Humboldt, State of California, described in Schedule "A" attached hereto and made a part hereof, said lands being described by tracts,



numbered separately in said Schedule. Said Schedule contains the estimated area of each separate tract and an estimate of the number of board feet of the redwood and Douglas fir timber contained therein, and except as otherwise provided in this Agreement, the area of such tract and the estimates of timber contained therein, as shown by said Schedule, shall, for all purposes herein, be conclusive and binding on the parties hereto.

2. The total purchase price is \$1,146,998.00, except as it may be modified by the provisions hereof.

3. The purchase price shall be paid in the following manner:

(a) \$50,000 on or before the execution of this Agreement. (Such \$50,000 has already been paid.)

(b) Minimum payments on July 1st of each year commencing with July 1st, 1947, to and including July 1, 1953, each of which minimum payments shall consist of \$100,000.00 in cash and a promissory note of Buyer payable to Seller or order, in the principal amount of \$56,714.00 payable July 1, 1954, with interest thereon at the rate of 4% per annum payable annually.

(c) In addition, Buyer shall pay Seller, prior to Buyer's removal of any timber from any numbered tract in Schedule "A" hereof, an amount equal to the total amount of M feet of redwood timber stated to be thereon in Schedule "A" hereof on the basis of \$3.00 per M feet, which such payment shall be credited against the next minimum cash payment



due under the provisions of paragraph 3 (b) hereof, and Buyer shall have no right to remove any timber from any tract described in Schedule "A" hereof unless Buyer has paid for said tract as provided in this paragraph.

(d) There is no balance as total of cash payments and notes is the purchase price.

The total purchase price to be paid hereunder shall not be reduced by reason of damage or destruction of any timber on the property sold hereunder which occurs subsequent to the date of this Agreement by reason of fire or other cause.

4. At any time prior to October 1, 1949, Buyer may select any tract or tracts described in Schedule "A" to be recruited. As such selections are made, but in no event later than October 1, 1949, Buyer shall name a cruiser and instruct him to proceed with the cruise. If the cruiser named by Buyer is acceptable to Seller, the total amount of redwood timber shown by such recruit shall be substituted in such tract or tracts for the amounts shown in Schedule "A" hereof and such substituted amount shall be final and be deemed thereafter to be actual amounts for all purposes of this Agreement. Such adjustment shall be made in the cash portion of the minimum annual payment next due. If the cruiser named by Buyer is not acceptable to Seller, Seller shall name a cruiser to make a joint cruise with Buyer's cruiser and the joint cruise shall then be final for all purposes herein. In the event the two cruisers cannot agree, they shall select a third

cruiser and the three cruisers shall make a joint cruise of all redwood timber then uncruised and the results thereof shall be final for all purposes herein.

5. Buyer stipulates that it has had access to the property of Seller covered by this Agreement, before the execution thereof, and that it is familiar with the land and topography thereof and the timber thereon and that the quality of said timber is fully known to it and that it is not making this Agreement by reason of any representation by Seller. It also stipulates that it shall not make any claim of any kind based on the quality or the kind thereof which it has the right to cut and remove under this Agreement, and Buyer likewise stipulates that it will not make any claim of any kind based upon the alleged shortage in the amount of timber which it has the right to cut and remove hereunder.

6. Seller shall have the right at all reasonable times, upon reasonable notice, to inspect the books and records and accounts of Buyer relating to its operations hereunder.

7. Seller agrees that in advance of Buyer logging on any of the property covered hereby, and, in any event prior to April 1, 1949, Seller will mark the exterior boundaries of the property covered hereby. Seller agrees that, without cost to Buyer, it will obtain right-of-ways for Buyer over and across the lands owned by Ward Redwood Company and Blue Creek Redwood Company in Humboldt and Del Norte Counties adjacent to or blocking access

to lands covered by this Agreement, and Seller shall obtain for Buyer the right to the use of any now existing roads on such lands owned by said two companies.

8. Whenever, and from time to time, lots or 40-acre pieces covered hereby have been paid for by Buyer pursuant to paragraph 3 (c) hereof, the Seller, upon request of Buyer, shall deliver to Buyer a grant deed covering such lots or 40-acre pieces. The minimum payments under paragraph 3 hereof shall not give Buyer credits under this paragraph.

9. When Buyer has paid the purchase price as provided in paragraph 3, Seller shall deliver to Buyer a grant deed to the property. Buyer may at any time pay the entire purchase price hereof, in which event the Seller, upon Buyer's request, will give Buyer a grant deed to the property covered hereby.

10. Whenever a deed is delivered to Buyer for any or all of the property covered hereby, Buyer agrees to pay Seller the taxes on such property so deeded, prorated to the date of such deed. Buyer shall pay any increase in taxes on any timber or logs covered hereby, which increase is the result of Buyer's operations hereunder.

11. This Agreement is subject to:

(a) An Agreement between Seller and California Barrel Company, Ltd., dated June 22, 1942, as amended by Agreements dated June 29, 1942, October 27, 1944, and October 31, 1944.

(b) An Agreement between Seller and Arrow Mill Company, dated June 15, 1943, as amended by Agreements dated April 26, 1944, and November 30, 1944, relating to Sections 11, 12, 13 and 14 of Township 12 North, Range 1 East, Humboldt Base, Meridian, Humboldt County.

(c) An Agreement between Seller and Arrow Mill Company, dated June 15, 1943, as amended by Agreements dated April 26, 1944, and November 30, 1944, relating to Section 7 of Township 12 North, Range 2 East, Humboldt Base and Meridian, Humboldt County.

(d) An Agreement between Seller and Arrow Mill Company, dated June 30, 1945, relating to Sections 8, 9, 15, 16, 17 and 18, Township 12 North, Range 2 East, Humboldt Base and Meridian, Humboldt County, all of the above agreements have been exhibited to and examined by Buyer.

(e) An Agreement between Seller and California Veneer Company dated October 4, 1944, relating to the South half of the Southeast quarter and the South half of the Southwest quarter of Section 13, the North half of the Northeast quarter and the North half of the Northwest quarter of Section 24, all in Township 12 North, Range 1 East, Humboldt Base and Meridian, Humboldt County, expiring November 10, 1947.

Seller warrants that there have been no extensions, modifications or changes in the terms of said Agreements other than above indicated. No exten-



sions, modifications or changes shall be made in said Agreements without the written approval of Buyer first had and obtained. All sums hereafter becoming due Seller under said Agreements for timber other than Douglas Fir and Spruce cut under the terms of said Agreements shall be credited to the next minimum payment becoming due.

Seller will, within ten days from receipt of written request from Buyer, give any notice which Seller has the right to give under the terms of any of said Agreements. If Seller fails to give such notice within the time prescribed, Buyer may either in its own name or the name of Seller give such notice.

In the event of failure to comply with the provisions of such notice within twenty days after the giving thereof, Buyer shall have the right in its name or in the name of Seller to enforce compliance with said notice and Agreements and take whatever action Seller would have the right to take under the terms of said Agreements, and to have credited upon the next minimum annual payment becoming due any money which may be due for damage to the property and timber purchased herein.

If Buyer gives such notice, it shall indemnify Seller in the event such notice is wrongfully given.

12. All operations conducted hereunder shall be conducted in accordance with all laws in force for fire prevention and control. Buyer agrees that good forestry practice shall be followed to the fullest possible extent.

13. Buyer agrees to do everything reasonably practical to protect the timber from fire, and in this regard:

(a) Buyer agrees to burn, under control and during favorable weather conditions, the slash and debris caused by its logging operations and thereby reduce the danger of fires getting beyond control and damaging standing timber.

(b) If Buyer uses steam donkey engines, Buyer agrees that all brush in the neighborhood of such engines shall be cleared to a sufficient distance to prevent any sparks or fire from the donkey engines setting fire to any neighborhood timber as provided by law.

(c) Buyer agrees to keep all logging camps and other structures used in connection with the operations hereunder, and the ground in their vicinity, in a clean, sanitary condition, and rubbish shall be removed and burned or buried and, when camps or other establishments are moved from one location to another, Buyer shall burn or otherwise effectively dispose of all debris and abandoned structures.

14. Buyer agrees to indemnify and save Seller harmless from any and all liability arising out of the cutting, felling, damaging or injuring of timber on property owned by a third party and arising from or relating to operations hereunder and from any and all liability of any kind or character whatsoever to third parties arising out of or relating to fires commenced or authorized to be commenced by



Buyer, its agents or licensees, or required by law or any public authority and connected with or relating to operations hereunder, and to indemnify and save harmless Seller from any and all liability of any kind or character whatsoever arising from or relating to the operations hereunder.

15. Buyer shall at all times observe and comply with, and cause its agents and employees to observe and comply with, all existing laws, ordinances and regulations pertaining to industrial accidents, public liability, Social Security, Fair Labor Standards Act, and Public Contract Act, as required by the laws of the State of California and the United States of America.

16. Any and all payments required to be made by Buyer hereunder, and all statements required hereunder, shall be delivered to Seller at its office at the Crocker Building, San Francisco, California, or at such other place as may from time to time be directed by Seller in writing.

17. Any notice to be given under this Agreement, or any communication to be made hereunder between the parties hereto shall be deemed to be given or made upon the deposit of the same in the United States mails by registered mail to be delivered to addressee only with postage thereon prepaid, duly addressed to the other party as follows:

Sage Land & Lumber Company, Inc.,  
Crocker Building,  
San Francisco, California;

Union Bond and Trust Co.,  
923 S.W. 5th Avenue,  
Portland, Oregon.

Either party shall have the right to give written notice to the other of a change in address, and after such written notification, such changed address shall be deemed for all purposes to be substituted in this Agreement for the address given above.

18. This Agreement shall be personal to Buyer and may not be assigned by Buyer without the written consent of Seller, except to A. K. Wilson or a Corporation controlled by A. K. Wilson, or his family. Upon such assignment or subsequent re-assignment and upon the assumption by the assignee of the Buyer's obligations herein contained, the assignor shall be relieved of the duty to perform such obligations. In the event of an assignment to a Corporation controlled by A. K. Wilson or his family, such assignment can be made only upon the written consent of Seller or, without such consent, if such Corporation has not less than \$100,000 paid in capital.

19. In the event that Buyer shall default in the payment of any sum of money required to be paid hereunder on any date whereon the same is due and payable, and such default shall continue for a period of 30 days, or in the event that Buyer shall default in any one or more of the provisions or Agreements herein contained other than for the payment of money, and such default shall continue for 30 days after notice thereof, then Seller may give to Buyer

30 days' notice of its intention to terminate this Agreement and thereupon, at the expiration of 30 days after receipt of such notice, this Agreement shall be void and of no effect and Buyer shall peaceably withdraw from said land and surrender the same to Seller, and Seller shall have and enjoy the said land as of its former estate, free and discharged of this Agreement, but Buyer shall nevertheless, remain liable to Seller as provided in paragraph 20 hereof. This covenant shall be deemed to run with the land, shall inure to the benefit of Seller, its successors or assigns, and shall bind Buyer and its Successors.

20. In the event that this contract shall be terminated because of the Buyer's default as provided for in paragraph 19, Buyer shall, nevertheless, remain liable to Seller pursuant to paragraph 14 hereof. It is agreed that all sums theretofore paid to Seller by Buyer shall be deemed liquidated damages for the breach of this Agreement, it being understood that it is impractical or extremely difficult, if not impossible, to ascertain the actual damage which Seller will sustain in the event of Buyer's default. In the event of such default and subsequent cancellations of this Agreement, the obligation of Buyer to make further payments shall cease.

21. Buyer shall be permitted to construct all roads desirable or necessary for the operations hereunder. Buyer shall have the right, upon request of Seller, to use any roads constructed upon lands of Seller constructed by others, providing access to the

property covered hereby, and Buyer agrees to pay its proportionate share of the maintenance and repair of such roads, in relation to its use thereof, provided that Buyer has first approved such expenditure in writing, and such approval will be given if such expenditures are reasonably necessary for the maintenance and repair of such roads.

22. If any dispute or disagreement shall arise in connection with the interpretation of this Agreement or the performance or non-performance thereof, or the existence or non-existence of any fact, and such dispute and disagreement shall not be settled in writing within 30 days after it shall have arisen, then it shall be settled by arbitration. One arbitrator shall be chosen by the party initiating arbitration, another arbitrator by the other party, and a third disinterested arbitrator by the first two arbitrators. The decision of the arbitrators shall be enforceable under the laws of the State of California.

Either party may initiate arbitration by giving the other written notice of its request for arbitration within 60 days after such dispute or disagreement has arisen, which notice shall state the matter to be arbitrated and the name and address of the arbitrator chosen by the party initiating arbitration. The party to whom such notice is given shall, within 30 days thereafter, choose its arbitrator and within said thirty days give written notice to the party initiating arbitration, stating the name and address of the second arbitrator. The two arbitrators so

chosen shall, within 30 days thereafter, select a third disinterested arbitrator. If the party requested to choose the second arbitrator fails to do so within the time specified, the arbitrator first appointed shall be sole arbitrator. In the event the two arbitrators do not select a third within 30 days after chosen, then the third shall be appointed by the judge of the Superior Court of the County in which the dispute arose. The party at fault shall pay the cost and expenses of the arbitration and if both parties are at fault, the expenses and cost of the arbitration shall be divided equally regardless of the extent of the fault of either party. If the arbitrators determine that neither party is at fault, the party initiating arbitration shall pay the cost and expense thereof.

Both parties shall have 30 days from and after receipt of notice of final determination of the controversy to perform this agreement in accordance with the award.

In any event, any award to be effective hereunder must be made within 120 days after notice of request for arbitration is given, unless the parties mutually agree to an extension.

23. In the event that Buyer is forced to suspend operations for more than thirty days by reason of fire, flood, strike, Acts of God, or other causes beyond its control, the provisions of this Agreement pertaining to minimum annual payments shall be suspended for the period of time that Buyer is unable to operate provided that no one extension shall be for more than six months and that there



shall be not more than a total of twelve months' suspension during the life of this Agreement. At any time Buyer's operations are suspended for more than thirty days, it shall immediately give Seller written notice thereof.

24. Time is of the essence of this Agreement.

25. The acceptance of Seller of one or more payments from Buyer after the date when such payment or payments becomes due shall not be considered or construed to be a waiver of the right of Seller to insist that any or all future payments be made within the time specified therefor and shall not be construed as a waiver of the right of the Seller to terminate this Agreement under paragraph 19 hereof, or a waiver of the provision that time is of the essence of this Agreement.

26. Seller reserves unto itself, its successors or assigns, right-of-way over the Ah Pah access road as now built and as hereafter built from the Redwood Highway to the Ah Pah Ranch at the mouth of Ah Pah Creek.

27. Seller reserves right-of-ways over property herein covered for two purposes as follows:

(a) To consummate reciprocal rights of way agreements with Ward Redwood Company and Blue Creek Redwood Company to permit access to property owned by Seller, Ward Redwood Company and Blue Creek Redwood Company, and

(b) To permit access to lands owned by Seller in the event this Agreement is terminated by reason of Buyer's default.



In the event of termination of this Agreement, Seller gives to Buyer right-of-ways over land owned by Seller to permit access to lands owned by Buyer.

28. Each and every provision of this Agreement shall inure to and be binding upon the successors and assigns of the Seller and the successors and assigns of the Buyer.

29. This Agreement supersedes all previous accompanying, contemporaneous or collateral agreements, options, stipulations, and understandings oral or written between the parties or their predecessors relating to the timber and property sold hereunder and is the only, and the entire agreement relating thereto between the parties hereto.

In Witness Whereof, the parties hereto have executed this Agreement as of the day and year first above written.

SAGE LAND & LUMBER COM-  
PANY, INC.,  
Seller,

/s/ E. O. HOLTER, JR.,  
President.

UNION BOND & TRUST COM-  
PANY,  
Buyer,

/s/ A. K. WILSON,  
President.

Duly verified.

## EXHIBIT No. 2-B

[Pencilled in top margin]: Extra copy with only part of page agreement attached.

## Agreement

This agreement made and entered into this 9th day of January, 1950, by and between Ah Pah Redwood Co., a California corporation, hereinafter called "Seller," and Coast Redwood Co., Incorporated, a California corporation, hereinafter called "Buyer."

## Witnesseth

Whereas, Seller has heretofore purchased the agreement dated December 13, 1946, between the Sage Land & Lumber Company, Inc., as Sellers, and the Union Bond & Trust Company, as Buyer and all rights thereunder, which agreement is known as the Sage "B" agreement, and Seller is now the full and complete owners thereof, and

Whereas, the Buyer has been logging in the district where the land covered by said agreement of December 13, 1946, is located, and have been logging the northwesterly part of the land covered by said agreement paying therefor \$5.00 per M. feet Board measure as stumpage for all the logs removed from said land as said logs have been removed, and

Whereas, the Seller hereunder has previously entered into two agreements with Walter Foster each for the sale of a part of the timber covered by said Sage "B" agreement, and

Whereas, the said two agreements entered into with Walter Foster which were later assigned to the Big Tree Timber Co., became in default and have been properly cancelled and terminated\* pursuant to the terms thereof, and

Whereas, it is desirable for the Seller to sell all of the land and timber being purchased under said Sage "B" agreement so as to receive stumpage payments therefor which will be of assistance in making the payments required to be made under said Sage "B" agreement, and also to liquidate their investment in said agreement, and

Whereas the Buyer is willing to enter into such an agreement and have sufficient logging equipment and facilities to successfully conduct such an undertaking, and

Whereas, the Buyer is operating a sawmill in the same County in which the timber is located, and

Whereas it appears to be to the best interest of those two corporations that this formal agreement be entered into.

Now, Therefore, in consideration of the premises and of the performance of the provisions of this agreement, the parties hereto agree as follows:

1. Seller agrees to sell and Buyer agrees to purchase and take from the Seller, at the times and upon the terms and conditions hereinafter set forth,

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[\*Underscored material appeared as an alteration on the original—initialed by A. K. W. and M.E.W.]

all the land and timber covered by said Sage "B" agreement situated in the County of Humboldt, State of California, more particularly described in Schedule "A" attached hereto and made a part hereof.

2. Buyer agrees to pay \$5.00 per 1,000 feet B. M. Humboldt scale for such lands and timber and are hereby given the option to pay therefor either on the basis of \$5.00 per 1,000 feet B. M. Humboldt scale on a pay-as-cut basis as the timber is removed from the land and/or pay for said land and timber on a cruise basis, or on a combination of either of such basis. When the land and timber are to be paid for on a cruise basis the payment for each tract as shown on Schedule "A" hereof is to be paid for at the rate of \$5.00 per 1,000 feet Board Measure for what timber is shown by schedule "A" hereunto attached to be on such tract. In any event, whenever Seller is entitled under the terms of said Sage "B" agreement to receive any deed or deeds to any of the land covered by the Sage "B" agreement, such land shall be forthwith deeded to Buyer or their nominee. When the logging has been completed on certain tracts of the land covered by the Sage "B" agreement and the remainder of the tracts covered by said Sage "B" agreement have been paid for on a cruise basis to the end that the land has either all been logged or all of the tracts described in Schedule "A" of said Sage "B" contract shall have been paid for, the Buyer hereunder shall be entitled to and shall forthwith receive a deed to all of the land covered under the Sage "B" agreement.

Time is of the essence of this agreement and when the payments are made on a stumpage basis, said payments are to be made on the 10th day of each month for all logs removed during the preceding calendar month.

3. It is understood that should the Buyer find it convenient or expedient to sell some of the tracts described in Schedule "A" of said Sage "B" agreement to a third party, Seller will forthwith secure from Sage Land & Lumber Co., a deed to said tracts as listed in Schedule "A" that are paid for and forthwith deliver to buyer or their nominee, a deed to the tracts so paid for. Buyer may sell one or more of said tracts on a cruise basis either for cash or on terms and upon payment being received by Seller therefor at the rate of \$5.00 per M. feet Board Measure, a deed therefor is to be issued to buyer or their nominee.

4. It is understood and agreed that all the terms and provisions of the Sage "B" agreement in respect to logging, shall be complied with and that all work shall be done in a good and workmanlike manner in keeping with good logging practices.

5. This agreement shall inure to the benefit of the successors and assigns of both Seller and Buyer.

In Witness Whereof, the parties hereto have executed this agreement the day and year first above written.

[Seal]

AH PAH REDWOOD CO.,

By /s/ A. K. WELSH,  
President;



By /s/ M. E. WILSON,  
Secretary.

[Seal] COAST REDWOOD CO.,  
INCORPORATED;

By /s/ A. K. WELSH,  
President;

By /s/ M. E. WILSON,  
Secretary.

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[Title of Tax Court and Cause.]

### MOTION FOR REVISION

Comes now your Petitioner, Ah Pah Redwood Co., acting by and through its attorney of record, James C. Dezendorf, and moves the Court for revision of its decision filed on September 28, 1956, in the above-entitled matter. The motion is based upon the following grounds:

#### I.

The opinion filed by the Court contains the following language:

“Whether or not petitioner’s theory be valid, its application will not constitute a disposition of the issue framed in the pleadings. Thus to narrow the issue is to make the unwarranted assumption that the timber involved in the transaction at issue constituted a capital asset to petitioner at the time of such transaction, within the definition contained in section 117 (a) (1) of the Internal Revenue Code



of 1939, or property used in petitioner's trade or business within the meaning of section 117 (j) (1), *supra*. In this connection, respondent makes the point, which we feel to be well taken, that petitioner at no time engaged in any logging activities, but, rather, merely sold the Sage timber to others under arrangements whereby the vendees would do the logging; that these sales of timber were the only business activity entered into by petitioner; that it is thus to be considered as having been engaged in the trade or business of selling timber; and that the timber in dispute, whether or not it was standing, was held for sale to customers in the ordinary course of such business.

“The facts found on this record lead to the conclusion that petitioner was engaged in the trade or business of selling timber and that the timber in controversy was held for sale to customers in the ordinary course thereof. Petitioner does not deny the nature of its business activity and the purpose for which the Sage timber was held. Nor does it claim that the timber comes within the definition of section 117 (a) (1), *supra*. In fact, petitioner bases its entire case upon the applicability of section 117 (j), *supra*. In this connection, petitioner's position is summed up in its statement on brief that section 117 (j) ‘\* \* \* includes timber to which section 117 (k) (2) is applicable and allows capital gain treatment of income therefrom without regard to the nature of the taxpayer's business or the purpose for which the timber is held.’ [Emphasis supplied.]

“The view thus expressed is in direct conflict with the plain wording of the statute relied upon. Section 117 (j), by its own language, specifically excludes from its operation all property held for sale to customers in the ordinary course of business. This being true, the gains derived from the sale of the Sage timber, regardless of the time of such sale, would not qualify for capital gains treatment under either section 117 (a) (1) or section 117 (j).”

The facts contained in the record are based upon a stipulation entered into between the parties, and adopted by the Court as a part of its opinion, and the testimony of three witnesses at the hearing of the cause, together with four exhibits introduced by Petitioner. The record contains no evidence to support a finding that Petitioner was engaged in the trade or business of selling timber and that the timber in controversy in this proceeding was held primarily for sale to customers in the ordinary course of business.

The law, as set forth in 26 USCA § 7453 and Tax Court Rule 31 (a), provides that the rules of evidence applicable to trials without a jury in the United States District Court for the District of Columbia shall apply to proceedings before the Tax Court of the United States.

The Tax Court may not make a finding of fact, and rest thereon a conclusion of law, when no evidence to support that fact is in the record.

In 39 Am. Jur. 146 (New Trial § 138), it is said:

“Where a cause has been tried by the court, its decision or finding has the same effect as the verdict of a jury, and if contrary to or not sustained by the evidence, a new trial may be granted. The question to be resolved by the appellate court is whether the trial judge, as a reasonable individual, acting as trier of the facts, could have found from the evidence such a verdict.”

To the same effect see *Parsons v. Federal Realty Corp.*, 105 Fla. 105, 143 So. 912, 88 ALR 275.

Upon the grounds herein set forth and the authorities cited in support thereof, your Petitioner therefore respectfully moves this Court to reconsider and revise its decision previously filed by deleting from said opinion the language quoted herein.

## II.

The record of the case fails to disclose that Regulation 29.117-7 was cited to the Court during the hearing held or in the briefs filed by the parties to this cause. During the years in question, that regulation read, in part, as follows:

“Reg. 111, Sec. 29.117-7. Gains and losses from involuntary conversions and from the sale or exchange of certain property used in the trade or business. \* \* \*”

Section 117 (j) provides that the recognized gains and losses

\* \* \*

“(c) From timber held for more than six months which is considered to have been sold under the provisions of section 117 (k) (2), and with respect to taxable years beginning after December 31, 1943, from timber owned or held under a contract right to cut for more than six months prior to the beginning of the taxable year which is considered to have been sold or exchanged under the provisions of section 117 (k) (1), regardless of whether such timber would be properly includible in the inventory of the taxpayer if on hand at the close of the taxable year or whether such timber was held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business,

shall be treated as gains and losses from the sale or exchange of capital assets held for more than 6 months if the aggregate of such gains exceeds the aggregate of such losses. If the aggregate of such gains does not exceed the aggregate of such losses, such gains and losses shall not be treated as gains and losses from the sale or exchange of capital assets.” [Emphasis supplied.]

On January 6, 1953, the Commissioner of Internal Revenue caused a modification to be made in the above-cited regulation, to reflect amendments to section 117 (j), Internal Revenue Code of 1939, effected by the Internal Revenue Act of 1951. The statutory amendment broadened the term “trade or business” to include unharvested crops, certain livestock, and coal. No change was made in the statute with regard to timber. The regulation, as modified,

omitted the language above cited. However, there is no ground for belief, nor has the Commissioner of Internal Revenue ever indicated, any change in the interpretation of the law as set forth in the previous regulation, nor has he so contended in this case, save for an implied reference in Respondent's brief filed subsequent to the trial of this cause (Resp. Br., pp. 13, 14).

Petitioner relied upon the above-quoted announcement and unchanged policy in presenting its case to this Court, and it is upon this basis that Petitioner now respectfully moves the Court to revise its opinion by deleting from its opinion previously filed the language quoted in ground I hereof, and substituting therefor the following:

“Petitioner is entitled to capital gains treatment of income derived from the disposal of timber, under the provisions of section 117 (j) and section 117 (k) (2), without regard to the nature of Petitioner's business or the purpose for which the timber is held, provided Petitioner satisfies the requirements set forth in the statutes cited.”

Wherefore, Petitioner respectfully moves this Court for revision of its opinion filed September 28, 1956, in the following particulars:

1. Deleting therefrom the language set forth in ground I hereof;
2. Substituting therefor the language set forth in ground II hereof;



3. Granting such other and further revision of its opinion as to the Court shall seem just and proper.

An opportunity to present oral argument is requested.

/s/ JAMES C. DEZENDORF,  
Attorney for Petitioner.

Received and filed October 29, 1956, T.C.U.S.

Entered November 5, 1956.

Served November 5, 1956.

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[Title of Tax Court and Cause.]

### ORDER ENLARGING TIME

For cause, it is

Ordered: That the time for filing the record on review and docketing the petition for review in the United States Court of Appeals for the Ninth Circuit is extended to March 18, 1957.

/s/ J. E. MURDOCH,  
Judge.

Dated: Washington, D. C., January 17, 1957.

Served January 18, 1957.

Entered January 18, 1957.



[Title of Tax Court and Cause.]

CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 12, inclusive, constitute and are all of the original papers on file in my office as called for by the "Designation of Contents of Record on Review" (including exhibits 1-A and 2-B, a part of the stipulation of facts), (but excluding documents requested in item 10, no action beyond ordering of briefs having been taken) in the case before the Tax Court of the United States docketed at the above number and in which the petitioner in the Tax Court has initiated an appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court case, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United States, at Washington, in the District of Columbia, this 29th day of January, 1957.

/s/ HOWARD P. LOCKE,  
Clerk, Tax Court of the  
United States.

[Endorsed]: No. 15,434. United States Court of Appeals for the Ninth Circuit. Ah Pah Redwood Co., a Corporation, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of Record. Petition to Review a Decision of the Tax Court of the United States.

Filed February 11, 1957.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

In the United States Court of Appeals  
for the Ninth Circuit

No. 15,434

AH PAH REDWOOD CO., a California Corporation,  
tion,

Appellant,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

NOTICE OF APPEAL

Notice is hereby given that Ah Pah Redwood Co., Appellant above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the findings and conclusions contained in the opinion of the Tax Court of the United States and the decision entered therein in this matter on September 28, 1956, and pursuant to Rule 29 of this Court has this day filed with the Clerk of the Tax Court of the United States a Petition for Review, a copy of which is attached hereto as Exhibit A.

/s/ JAMES C. DEZENDORF,  
Attorney for Appellant.

[Endorsed]: Filed December 15, 1956, U.S.C.A.

[Title of Court of Appeals and Cause.]

STATEMENT OF POINTS ON WHICH  
APPELLANT INTENDS TO RELY ON  
APPEAL

Points

The points on which Appellant Ah Pah Redwood Co. intends to rely on appeal are as follows:

I.

The Tax Court erred in its opinion, wherein it made the following statement:

“The facts found on this record lead to the conclusion that petitioner was engaged in the trade or business of selling timber and that the timber in controversy was held for sale to customers in the ordinary course thereof. \* \* \*”

Error is predicated on the ground that the record shows no stipulated fact or evidence upon which such a conclusion can be based.

II.

The Tax Court erred in its opinion, wherein it made the following statement:

“\* \* \* In this connection, petitioner’s position is summed up in its statement on brief that Section 117 (j) ‘\* \* \* includes timber to which Section 117 (k) (2) is applicable and allows capital gain treatment of income therefrom without regard to the nature of the taxpayer’s business or the purpose for which the timber is held.’ [Emphasis supplied.]

“The view thus expressed is in direct conflict with the plain wording of the statute relied

upon. Section 117 (j), by its own language, specifically excludes from its operation all property held for sale to customers in the ordinary course of business. This being true, the gains derived from the sale of the Sage timber, regardless of the time of such sale, would not qualify for capital gains treatment under either Section 117 (a) (1) or Section 117 (j).”

Error is based upon the long-established interpretation of 1939 IRC Sec. 117 (j), both by Congress and by the Commissioner of Internal Revenue, and based upon the regulations promulgated by the Commissioner of Internal Revenue and in effect during the years involved in this controversy.

### III.

The Tax Court erred in its opinion, wherein it stated:

“While there is no direct evidence of the precise terms of the oral cutting contract entered into between petitioner and Coast, such contract, for aught that is shown, looked immediately to the severance and removal of all timber standing upon the Sage Tract.”

The Court erred in its determination in that the so-called oral contract between Appellant Ah Pah Redwood Co. and Coast Redwood Co. is an oral license to enter and to cut timber, revocable at will, and does not constitute a disposal of timber under the terms of 1939 IRC Sec. 117 and the regulations promulgated thereunder until such time as the licensee actually cuts and removes the timber.



## IV.

The Tax Court erred in its opinion, wherein it stated:

“The evidence here affords us no basis for making any finding that petitioner at any time in the taxable years knew or even suspected that its prior estimate of standing timber was erroneous. Albeit such error was readily ascertainable, it was not in fact ascertained at any time within either of the taxable years. In our view, therefore, the revision sought by petitioner does not qualify under the statutory provision that the allowance ‘for subsequent taxable years shall be based upon such revised estimate.’ ”

The Court failed to distinguish between adjustment of the depletion unit in subsequent years and the revaluation of the property for determination of the depletion basis, because of misrepresentation, fraud or gross error. The contention of Appellant is based upon the theory that property must be revalued for basis purposes because of gross error, misrepresentation or fraud as provided in 1939 IRC Sec. 23 (m) and regulations promulgated thereunder.

Respectfully submitted,

KOERNER, YOUNG, McCOLLOCH & DEZENDORF,

/s/ JAMES C. DEZENDORF,

/s/ [Indistinguishable].

Duly verified.

[Endorsed]: Filed February 19, 1957, U.S.C.A.